6 Dirty Secrets Your Broker Isn't Telling You

Description

Many investors think their stock brokers have their best interests at heart. After all, if your account balance goes up, chances are your broker will inevitably get more in fees, whether they're from trading stocks or assets under management.

Unfortunately, it's not quite that simple. In fact, chances are that your broker is encouraging you to make moves that might not be in the best interest of your money. Here are six ways the big guys on Bay Street are hosing smaller investors.

Short-term thinking

It's hard to make money by actively buying and selling stocks. Taxes and transaction costs are killer.

Bay Street is run on fees. The more that brokers can encourage you to trade, the better. Paying $9.99 per trade might not seem like much–especially if you have many thousands of dollars in your account–but those trades really add up. A million customers trading just once a week will rack up half a billion dollars in commissions annually, all while most likely underperforming the market.

Margin

I don't want to say that borrowing to invest is a silly concept, because there are plenty of times when it makes sense. Much of it depends on the interest rate paid.

Depending on your broker, charges to borrow on margin range from approximately 3% to 6% annually. At the lower end of the spectrum, it might make sense to borrow. At the higher end, it almost never does.

Most brokerages view margin as a profit centre. They're happy to lend money that's almost guaranteed to get paid back at rates higher than you'd pay for a mortgage. It's good business on their part.

The next big thing

Brokers like to get their clients excited about the next big thing. Whether it's technology, energy, or the newest spin on a mature industry, chances are that your broker has told you about it.

But there's a huge difference in being able to predict a new trend and being able to profit from it. With dozens of different tech companies lining up to get in to the next sexy growth market, which one will eventually conquer it? Nobody really knows.

Don't look far

Your online broker can't really tell you to invest in its parent company. You'll never see bullish statements about other banks on the website either, since the last thing it wants to do is remind you there are competitors.

But brokers have been great investments in the past and should continue to be in the future. Sure, a company like **Royal Bank of Canada** (TSX:RY)(NYSE:RY) is much more than wealth management, but it's not like the other things a bank does will ever go out of style. We always need access to capital.

Dividends are afterthoughts

Many brokers treat dividends as an afterthought, barely mentioning them to investors who are much more interested in capital gains.

But according to studies done in the U.S., dividends have accounted for between 80% and 90% of the market's return over the last century. Reinvesting those dividends would have been the difference between lacklustre returns and spectacular ones.

One dividend stock I think looks attractive at today's levels is **Shaw Communications Inc.** (TSX:SJR.B)(NYSE:SJR). The company has announced a transformational acquisition to get it into the wireless space. It also holds a dominant position in western Canada's cable and Internet market, which is the kind of sticky revenue investors like to see. And its 5.1% dividend is very attractive as well.

How to be successful

There's a reason why Warren Buffett, the greatest investor of all time, says his favourite holding period is "forever." It's because it works.

Successful investing comes down to buying great companies at reasonable prices and holding them for a long time, letting compounding do its magic.

One example of that has been **Dollarama Inc.** (TSX:DOL). Dollarama has a clear moat, plenty of growth potential, even after opening 1,000 stores coast to coast, and has successfully expanded its price point from $1 to up to $3.

Since its 2009 IPO, shares have been on fire, rising nearly 650%–and that's even after recent weakness. I can't guarantee it'll perform that well over the next five years, but the story still looks intact. There's little reason to sell today and have to pay the taxes.

CATEGORY

1. Dividend Stocks
2. Investing

TICKERS GLOBAL

1. NYSE:RY (Royal Bank of Canada)
2. NYSE:SJR (Shaw Communications Inc.)
3. TSX:DOL (Dollarama Inc.)
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